

Russian WTO Accession:

What Has Been Accomplished, What Can be Expected

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Abstract

This paper summarizes the principal reform commitments that Russia has undertaken as part of its World Trade Organization (WTO) accession negotiations, providing detailed assessments in banking, insurance, and agriculture. The paper assesses the gains to the Russian economy from these commitments, based on a summary of several modeling efforts undertaken by the author and his colleagues. The author compares

Russian commitments with those of other countries that have recently acceded to the WTO to assess the claim that the demands on Russia are excessive due to political considerations. He explains why Russian WTO accession will result in the elimination of the Jackson-Vanik Amendment against Russia. Finally, he discusses the remaining issues in the negotiations and the time frame for Russian accession as of the fall of 2007.

This paper—a product of the Trade Team, Development Research Group—is part of a larger effort in the department to assess the impact of WTO accession on the development and poverty reduction of developing and transition economies. Policy Research Working Papers are also posted on the Web at <http://econ.worldbank.org>. The author may be contacted at dtarr@worldbank.org.

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I. Introduction

As of May 2007, there are 150 member countries of the World Trade Organization (WTO). Trade among them represented 97 percent of the world's trade turnover, including over 94 percent of the foodstuffs. Russia is the largest economy outside the WTO and—along with Azerbaijan, Belarus, Kazakhstan, Tajikistan, Ukraine, and Uzbekistan of the Commonwealth of Independent States (CIS)—is among the 29 countries that were attempting to accede to the WTO in early 2007.

The Working Party on accession of the Russian Federation to the WTO was established June 16, 1993.. The WTO Working Party on Russia's accession comprises 60 countries (with the addition of two new WTO members, Vietnam and Cambodia), and is the largest such Working Party in the history of the WTO . By March 2006, the Working Party had met 30 times. By the spring of 2007, Russia has successfully concluded bilateral agreements with all but the two new members of its Working Party and Georgia.² The focus now is on the multilateral phase of the negotiations, where the parties indicate a lot of work remains to be done as of the spring of 2007.

In the paper, I address several issues regarding Russian WTO accession. In section II, I explain what Russia will get from WTO accession. In section III, I summarize the principal Russian reform commitments at the WTO. In section IV, I address the question of whether the demands on Russia are excessive due to political considerations. In section V, I explain why Russian WTO accession will result in the elimination of the Jackson-Vanik Amendment against Russia. In the final section, I discuss remaining issues in the negotiations and the time frame for Russian accession.

II. WTO Accession for Russia: A Crucial Historical Opportunity

WTO accession is a process that may be used as an important tool for economic development. WTO accession will impact on a wide range of policies and institutions, including tariff policy, customs administration, standards, rights of foreign investors (especially in services), agricultural policy, intellectual property and possibly government procurement. It therefore represents a time for evaluation of a very wide range of regulation and an opportunity to implement important trade, foreign direct investment

² No significant problems are anticipated that would prevent agreements with Cambodia or Vietnam. Georgia earlier had agreed to a bilateral agreement on Russian WTO accession but has withdrawn from that agreement due to a deep dispute discussed below.

and institutional changes. These changes can move the economy toward an open trade and investment model of economic development and away from an import-substitution economic model.

My colleagues and I have undertaken several detailed numerical studies to assess the consequences of WTO accession in Russia. (See Jensen, Rutherford and Tarr, 2006, 2007; Rutherford, Tarr and Shepotylo, 2005; and Rutherford and Tarr, 2006, forthcoming.)³ We have assessed the likely impacts on overall income, wages, returns to capital, poverty, output, exports, imports and employment by sector, and how impacts will differ across the regions of Russia. The basic macroeconomic impacts are presented in table 1. What I would like to emphasize is that these studies indicate that Russia will reap substantial gains from WTO accession, the benefits are widespread and will reduce poverty, those regions that establish a better investment climate will reap greater gains from WTO accession, and, crucially, most of the gains are due to Russia's own reforms. The reforms in the services sectors, are the most important of Russia's own reforms.

Although governments typically try to sell WTO accession to the general public as a process that will yield increased market access for their own exporters, our estimates are that less than 10 percent of the gains come from improved market access for Russian exporters. After all, Russia has negotiated most favored nation status or better with all its significant trading partners. While Russian exporters will be accorded additional legal benefits in antidumping cases once Russia is a WTO member, and this is the source of the gains we estimate, many economists are cynical regarding the fairness of antidumping proceedings. This suggests that we should not expect very significant differences in determinations against Russian exporters in antidumping cases, and consequently improved market access in export markets cannot be the source of significant gains to Russia from WTO accession.⁴

Given that the benefits to Russia of WTO accession come from its own internal reforms, some infer from this fact that Russia will gain little from WTO accession—since Russia could unilaterally implement these reforms. There are several reasons why I take the opposite view—that the process of WTO accession is a unique historical opportunity to achieve reform.

³ Versions of all these studies are available at www.worldbank.org/trade/russia-wto. This work follows my earlier studies examining Russian trade policy. See Tarr (1993, 1994, 1999, 2002) and Michalopoulos and Tarr (1994, 1996, 1997).

⁴ In addition, members of the WTO obtain rights in international trade. Members are granted permanent most-favored nation status to the markets of other member states. So Russia will not have to be concerned about annual renewals of Most Favored Nation status. Members are also able to use the WTO's dispute settlement procedures to protect their trade interests, such as in antidumping cases. Trade disputes among WTO members are resolved based on WTO legal agreements under which smaller countries have the potential to win disputes against large countries. All WTO agreements require unanimous consent of all the members, and this helps provide a voice for the smaller member countries. On the other hand, non-members will be influenced by the new rules of this dominant organization in international trade, without a voice in their formation.

The key reason that WTO is important is the political economy dimension. Given the concentrated benefits to industries that achieve protection, industry groups will typically lobby for protection. On the other hand, since the benefits to consumers are diverse and less concentrated, they typically do not lobby against protection, but hope others with similar interests will lobby on their behalf. This so called “free rider problem” in political decision-making results in an absence of representation of the views of the consumer and broader economic interests in political discussions of tariffs. Lobbying and political economy considerations often allow special interests to strongly influence policy so that reforms are slow. WTO accession, however, requires across the board reform in many sectors, and the pressure of a WTO negotiation engages policy makers at the highest levels of government. Experience has shown that high-level policy-makers, who have the economy-wide interest in mind, will often intervene to impose reform on slow moving Ministries. In the case of Russia, the process began to move when Putin made WTO accession a priority in his first term.

In section III, I summarize many of the key reforms that Russia has made. It is difficult to argue that Russia would have made reforms as widespread and as deep as it has without the external pressure of WTO accession. Reforms are accomplished in the context of WTO accession that would not normally be achieved so quickly. That is, WTO bindings and external pressure make it easier for a government to adopt a trade policy designed to promote growth and poverty reduction. Moreover, unlike unilateral reforms, once a country commits to a reform at the WTO, it is bound by an international commitment that is difficult to reverse in the future by a less reform minded government. I conclude that the process of negotiating bilateral market access with the countries on its WTO Working Party on Accession, has led to a dramatic increase in reforms regarding the Russian trade and foreign investment regimes, and thereby has helped Russia move toward an open economy model of economic development.

III. Russian Commitments to Foreign Exporters and Investors⁵

Non-Agricultural Market Access (NAMA)

Overall Tariffs. Russia agreed to reduce its bound MFN tariffs to about 8 percent on average. How does this compare to recent levels of tariffs in Russia? Russia’s tariff schedule contains over 11,000 tariff lines. On about 1,700 of these, the tariff is written as: “x percent, but not less than y euros.” That is, a specific tariff of y euros per unit applies if the specific tariff exceeds the ad valorem tariff. This amounts to applying the maximum of either the specific or ad valorem tariff. Previous calculations of Russia’s tariffs have either inappropriately ignored the specific tariffs that often apply or have

⁵ The United States Trade Representative (2006) has released five “Fact Sheets” with details of Russian commitments as part the US-Russia bilateral protocol. See this source for further details.

been based on a minority of the tariff lines (those available in the printed data of the Russian Customs Service).⁶

Recently, however, Oleksandr Shepotylo and I (see, Shepotylo and Tarr, forthcoming) have obtained data that allowed us to calculate the actual Russian tariffs. Briefly, our key results are the following. The average tariff in Russia has increased between 2001 and 2003 from about 11.5 percent to between 13 and 14.5 percent, but it has held steady in 2004 and 2005. This places Russia's tariffs at a level slightly higher than other middle-income countries and considerably higher than the OECD countries. The tariff structure became much more diverse between 2001 and 2003, but the dispersion of the tariff moderated in 2004 and 2005. Notably the trade weighted standard deviation of the tariff approximately doubled from 9.5 percent in 2001 to 18 percent in 2003, but then fell to 15.2 percent by 2005. "Tariff peaks," that is, tariff lines with very high tariffs, are more of a problem in 2005 than in 2001, but less so than in 2003. The reason for the increase in the tariffs is the specific tariffs, as the ad valorem rates have not increased. More tariff lines are subject to specific tariffs in 2003-2005 than in 2001, and the appreciation of the euro, relative to 2001 has increased the ad valorem equivalent of the specific tariffs. The food sector and light industry are the aggregate sectors with the highest tariff rates—their tariff rates in 2005 were 23.1 percent and 19.5 percent on a trade-weighted basis. At the two digit level, motor vehicles, footwear, leather products and sugar are among the most highly protected.

Our aggregate results are summarized in table 1. For the most recent year, Russia's MFN tariffs were about 12.1 percent on a simple average basis or 14 percent on a trade weighted basis in 2005, where we have taken into account the ad valorem equivalents of Russia's specific tariffs. We find that ignoring the specific tariffs results in a reduction in the calculated average tariff to about 11 percent. Independent of how the members of the Working Party have calculated Russian tariffs, an average Russian tariff of the 8 percent implies a decline.

Civil Aircraft and Capital Goods and Equipment. One of the more contentious areas of tariff negotiation was civil aircraft. Tariffs on wide body aircraft will be reduced from 20 to 7.5 percent in the four years following accession. Russia has agreed to substantial tariff reductions in construction, agricultural and scientific equipment, as well as medical devices. Tariffs in these sectors will average 5 percent.

Services Commitments

Some of the most important and internally controversial commitments by Russia are in the area of services.

Insurance. Russia will significantly increase its commitments to multinational insurance providers. It will allow 100 percent foreign ownership of non-life insurance

⁶ The annual report of the Russian Customs Service publishes trade data for about 1600 tariff categories. There are over 11,000 tariff lines, so the Customs Service aggregates many tariff lines in this publication.

companies upon accession to the WTO. Russian prohibition of foreign participation in mandatory insurance lines as well as Russian restraints on the number of licenses granted to foreign life insurance firms will be phased out five years after the date of accession. Russian had restrained the amount of foreign investment in the sector to be about 15 percent of total investment; but as part of its accession commitments, Russia agreed to increase this limit to 50 percent.

The Russian banking and insurance sectors see themselves as very vulnerable to much more powerful and efficient multinational providers of financial services. As such they were strong opponents of commitments in these sectors. The insurance sector was reportedly very concerned by the level of commitments made by their government in the rush to get an agreement prior to the G-8 conference in Saint Petersburg in late spring 2006. The experience of China, where similar fears were expressed by insurance interests, is instructive and suggests that these fears are exaggerated. Prior to 2001, China had a very closed insurance market. As part of its WTO accession commitments, China agreed to gradually remove restrictions on foreign investors in insurance and fully open its insurance markets by January 2005 (except foreign companies could hold a maximum of 50 percent in the life insurance market; (see Mattoo (2003, p. 312). As expected the results have been extremely positive for consumers of insurance services in China. In addition, wages of skilled workers in the insurance sector have grown, and even domestic insurance companies have grown, due to better access to foreign capital as foreign investors, with only one exception, have sought and obtained local partners.⁷.

⁷ The key developments in the insurance sector since China's accession to the WTO in 2001 are: (i) very strong growth of both domestic Chinese and foreign insurance companies operating in China; (ii) continued dominance of the market by Chinese companies; (iii) large increase in employment of skilled workers in the sector; (iv) entry by foreigners through either joint ventures or strategic investment in Chinese companies; and (v) acquisition of foreign capital by Chinese companies through strategic partnerships.. Total premiums have more than doubled between 2001 and 2005. During this time, the total number of insurance companies has increased from 41 to 78, and the number of Chinese companies increased from 20 to 41. (Facts on the Chinese insurance market for this note are taken from primarily from Ewing (2006) and supplemented from Datamonitor (2005).)

The largest insurance market in China is life insurance, which captures about two-thirds of the total insurance premiums in China. The life insurance industry in China has more than doubled from 2001 to 2005, and forecasts are for continued growth in the market that will likely double the size of the market by 2010. Life insurance premiums increased from 140 billion yuan (\$17.5 billion) in 2001 to 365 billion yuan (\$45.4 billion) in 2005. Demand for actuaries, underwriters and managers has soared, e.g., the industry added 500,000 new agents to bring the total to 1.5 million. The life insurance market remains dominated by domestic companies, especially three large domestic Chinese companies: The domestic share of the market was 91 percent in 2005, down from 97.5 percent in 2004. Most of the domestic life insurance companies have taken on a strategic foreign investor (like HSBC, Zurich Financial Services, Meiji Life Insurance and the Carlyle Group), as these investors now own minority shares of the companies, with shares ranging from 1 percent to 25 percent. In 2006 there were 22 foreign life insurance companies operating in China, but 21 of these were joint ventures with Chinese companies. Thus, there is a very strong pattern among foreign life insurance companies to either form a joint venture with a Chinese company or else to purchase a minority strategic interest in a Chinese run company. Only American International Group sells life insurance in China independently of a Chinese partner.

Banking and Securities. Russia has agreed to bind most existing market access arrangements and to offer some additional liberalization. These commitments include: allowing 100 percent foreign ownership of banks and other non-insurance financial institutions; allowing cross border provision of numerous services including asset management services, credit cards and other types of payments; allowing foreign investment companies to own and trade the full range of securities available in Russia, including state securities and bullion, and to participate in the financing of privatization of state owned enterprises. In addition, Russian restraints on the share of the sector captured by foreign banks will increase from about 15 percent of total investment to 50 percent.

In banking, opposition galvanized around the branch banking issue. Russia was willing to allow subsidiaries of international banks. Subsidiaries must be registered as Russian entities, have their own capital and are subject to supervision by the Russian central bank. Branches, however, do not have a separate legal status or capital apart from their foreign parent bank. In general, entry into banking services in a country is easier when branches are permitted and the U.S. Treasury has been attempting to assure branch banking is permitted in all countries admitted to the WTO. The Russian central bank maintained that it could not regulate or supervise branches adequately and that depositors would therefore be at risk.

The counterargument to the view of the Russian central bank is that theory suggests and experience has shown that multinational banks have more of their reputation on the line with a branch, and this will provide greater incentive to avoid default. Moreover, to the extent that the costs of entry through branches are smaller, the number of multinationals present will be larger with branches. Then the host country has the advantage of a larger amount of FDI if it allows branches. This is the greatest advantage of allowing branch banking, but it was also the greatest concern of the central bank of Russia--since it implies greater potential adjustment costs for Russian banks.

Of the 150 countries in the World Bank database on "Banking Regulation and Supervision" for 2003,⁸ branch banking was prohibited in only 18. The 18 countries prohibiting branch banking were: Russia, Kazakhstan, Azerbaijan, Belarus and Ukraine from the CIS plus Bolivia, Botswana, Columbia, Costa Rica, Macedonia, Malaysia, Mexico, Nigeria, Papua New Guinea, Philippines, Serbia and Montenegro, Trinidad and Tobago and Zimbabwe. The remaining 132 countries, including all OECD and EU (25) countries allow branch banking.

It seemed that the Chinese approach offered a reasonable compromise. China allows branches, but China imposes a large minimum asset requirement on the parent bank.⁹ The de facto consequence of this is that China only allows rather large multinational banks to enter. This both protects incumbent Chinese banks against many

⁸ See http://www.worldbank.org/research/projects/bank_regulation.htm. Rows 31, 32 and 42 provide data on branch banking.

⁹ This minimum asset requirement would have to be scheduled in the GATS commitments in order to avoid disputes with members.

new entrants, but also means that the foreign entrants are likely to be relatively safe and in need of little supervision or regulation

Banking interests in Russia succeeded in getting Putin himself to say that branch banking was a deal breaker for Russian WTO accession. Based on its bilateral agreement with the U.S., Russia succeeded in avoiding a commitment on branch banking, becoming the only non-LDC acceding country to avoid such a commitment.¹⁰ Like many items in accession negotiations, succeeding in avoiding a commitment is a pyrrhic victory as Russia will lose the benefits from greater foreign direct investment. Nonetheless, multinational banks, operating as subsidiaries, have greater market access and national treatment rights under the bilateral U.S.-Russia agreement and Russia should benefit from greater involvement of multinational banks in Russia over time .

Telecommunications. As part of its bilateral agreement with the European Union, Russia agreed to terminate the monopoly of Rostelekom on fixed line long distance telephone services. In the agreement with the U.S., Russia committed to allow 100 percent foreign owned telecommunications companies to operate in any telecommunications sector. Russia also agreed to implement the WTO Basic Telecommunications Reference Paper, which among other reforms will require Russia to establish an independent regulator and provide for transparency and interconnection obligations. Presently the Ministry of Communications is responsible for managing any state assets as well as performing regulatory functions such as interconnection and licensing. Conflicts of interest are more likely when the same government entity that manages the state assets is also responsible for the regulatory functions,¹¹ and it is likely that a commitment to an independent regulator and other key reforms in the sector would not have been achieved without international pressure

Business Services. Russia will ensure market access and national treatment for a wide variety of professions, including lawyers, architects, accountants, engineers, health care professionals, advertising, marketing and management specialists. Foreign companies will be permitted to operate as 100 percent foreign owned entities.

Distribution Services. Russia will allow 100 percent foreign owned companies to engage in wholesale, retail and franchise sectors, as well as express delivery services upon accession to the WTO. This includes distribution of pharmaceuticals, with minimal limitations.

Agriculture Issues

Agricultural issues have been among the most contentious in Russia's WTO accession negotiations. The key unresolved issue is agricultural subsidies. Russia,

¹⁰ Russia agrees to reopen discussions on this issue upon consideration of membership in the OECD.

¹¹ As a result of proceedings in a Swiss arbitration court, questions have arisen of indirect financial links between the Russian Minister of Communications and Megafon, the country's third largest mobile telephone provider. No links have been proven, however. See Oleg Dorman, "Communication Minister Reiman Admits his Connection to Megafon," Moscow News, April 5, 2007.

however, has made considerable commitments in market access as well as sanitary and phyto-sanitary negotiations. For beef, pork and poultry exports, the disputes with the U.S. were among the most significant. The bilateral agreement with the U.S. details the following commitments.

Market Access. Russia agreed to bind its tariffs on all agricultural products. In many cases this entailed tariff cuts from present levels. See U.S. Trade Representative (2006) for details.

Non-Tariff Barriers. Regarding poultry and pork products, instead of joint inspection of facilities, Russia agrees to allow the U.S. Department of Agriculture-Food Safety and Inspection Service to inspect and certify new facilities or facilities that need to remedy a deficiency. Regarding beef, Russia and the U.S. agree to timely joint inspections of all facilities that will export to the Russia. Once a joint inspection has been completed, the inspection process applying to poultry and pork exporters will apply.

Regarding trichinae in pork, Russia will allow freezing as mitigation of the risk on sales destined to Russian consumers. Previously, Russia only allowed this for intermediate pork sales. The Russian regulatory regime in modern biotechnology products has been unpredictable. For example product registrations and approvals in the area of feeds were halted in 2004 when work began on a new permanent regulatory system. Russia also agreed to maintain an interim approval and registration system for modern biotechnology products (until a permanent one can be established) that is science based, transparent and consistent with the WTO Agreement.

IV. Are there Excessive Demands on Russia due to Political Considerations

The allegation that demands on Russia are either political or excessive by the standards of other countries that have acceded to the WTO have been repeated frequently and have been come to be believed by many observers. I believe, however, that the evidence contradicts this allegation. Aside from a couple of well publicized cases where unusual demands were placed on Russia,¹² the demands placed on Russia are typical of the WTO accession process in the past ten years. The process of acceding to the WTO since 1998 is a difficult one in which all acceding countries have been asked to take on very significant commitments to foreign exporters and investors. In comparison with the commitments of these countries, the commitments that are reported for Russia do not appear excessive.

Goods. In goods, Russia has agreed to bind its tariffs at an average tariff level of 8 percent, after an adjustment period (USTR, 2006). This is a slightly higher average bound tariff on goods than most countries that have acceded to the WTO since 1998 (see WTO, 2005). The average tariffs for other acceding countries are: Saudi Arabia, 10.5 percent; Former Yugoslavian Republic of Macedonia, 6.2 percent; Armenia, 7.5 percent;

¹² One unusual demand on Russia was the pressure on Russia to unify its domestic and export price of natural gas. This demand, which occupied negotiators for considerable time and was eventually dropped by the European Union, would have imposed a very high cost on Russia (see Tarr and Thompson, 2005).

Chinese Taipei, 4.8 percent; China, 9.1 percent; Moldova, 6.0 percent; Croatia, 5.5 percent; Oman, 11.6 percent; Albania, 6.6 percent; Georgia, 6.5 percent; Jordan, 15.2 percent; Estonia, 7.3 percent; Latvia, 9.4 percent; Kyrgyz Republic, 6.7 percent.¹³ Thus, by the standards of countries that have acceded to the WTO in the last eight years that are not “Least Developing Countries,” Russia appears to have acceded with bound tariffs slightly higher than average, i.e., no excessive demands from the Working Party here.

Services. In the area of services, no simple measure like an average tariff is available. But an examination of the table of commitments of the countries that have acceded to the WTO since 1998 (WTO, 2005, table 5) shows that all of them have assumed a rather high and comprehensive level of commitments, in terms of sectors included. On a qualitative basis, the more detailed discussion above on banking and insurance does not suggest an above average level of commitments in these important sectors. On the contrary, Russia has been able to avoid a commitment to branches of banks, unlike almost all of these countries.

Agriculture. Although trade-distorting subsidies (subsidies that are dependent on exports or production) are constrained by the WTO, the WTO allows without any constraints publicly funded subsidies to agriculture that are not trade-distorting. These types of subsidies are known as “Green Box” subsidies. Green Box subsidies include a wide range of publicly funded measures including research and development, pest control, general and specialist training, extension and advisory services, inspection services for health and sanitary reasons, marketing and promotion services, infrastructure services, including electricity, roads and environmental expenditures, targeted support to low income population through food stamps or subsidized prices, direct payments to producers to support income provided it has minimal trade-distorting features, crop insurance subsidies for natural disasters, adjustment assistance through producer retirement programs and indirect income support not related to prices. The world-wide trend is to move agricultural support away from trade-distorting subsidies toward Green Box measures. In part, this is because it is generally recognized that trade-distorting subsidies are a highly inefficient way of helping agricultural producers compared with Green Box measures. And Green Box measures are more effective at creating a competitive agricultural sector in the long run.

Nonetheless, incumbent members of the WTO, like the European Union, Canada, the United States and Norway, have a base period for trade-distorting agricultural subsidies that allows considerable trade-distorting subsidies. The precedent among acceding countries, however, is that the three year period prior to accession forms the base period for permitted trade-distorting subsidies, and trade-distorting subsidies are negotiated down from that base. Although it is good for the Russian economy, the problem for Russian WTO accession negotiators is that in recent years Russia has had a rather low level of trade-distorting agricultural subsidies; but Russia would like to retain the right to U.S. trade-distorting subsidies in agriculture in the future. This issue was not resolved during the bilateral phase of the negotiations and will be one of the most

¹³ Two of the “Least Developed Nations” acceded with relatively high bound tariffs: Cambodia, 17.7 percent; and Nepal, 23.7 percent. But the WTO accords a preferential status to developing countries.

contentious in the multilateral phase. Other countries, like Kazakhstan, who have a similar negotiating position, are waiting to see if Russia is successful in its negotiations. If Russia is able to obtain the right to provide trade-distorting subsidies in agriculture on a new basis among acceding countries, these other countries will demand parallel treatment. In any event, it is difficult to argue that Russia is being treated more harshly than other countries that have acceded, since it is asking for a departure from precedent.

V. Russian WTO Accession and the Jackson-Vanik Amendment

The Jackson-Vanik Amendment of the U.S. requires an annual review of Russian emigration policies in order for the U.S. to grant Most Favored Nation (MFN) status to Russia (and other former communist countries). This is a significant irritant to Russia, but the U.S. does not presently have any commercial pressure on it to remove Jackson-Vanik. Once Russia becomes a WTO member, however, there will be commercial pressure on the U.S. from its own exporters and investors to remove Jackson-Vanik. Consequently, the U.S. will almost certainly remove Jackson-Vanik after Russian WTO accession.

The WTO requires that permanent MFN status be granted to all members. Thus, the provisions of Jackson-Vanik are inconsistent with MFN treatment required by the WTO. The U.S. has two options once Russia becomes a member of the WTO: (1) eliminate Jackson-Vanik; or (2) invoke the "non-application principle" of the WTO. For newly acceding countries, a member of the WTO can opt out of WTO commitments with respect to the newly acceding country if it invokes the "non-application" principle. If the U.S. were to invoke the non-application principle against Russia, it means that the U.S. would refuse to honor its WTO obligations to Russia. But non-application is reciprocal. So the U.S. would not have any assurance that its exporters or investors would be treated in Russia according to Russia's WTO commitments.

In practice, the U.S. has dropped Jackson-Vanik on all countries that have acceded to the WTO with one exception. In the cases of Albania, Bulgaria, Cambodia, Estonia, Latvia and Lithuania, Jackson-Vanik was repealed prior to accession. In the cases of Mongolia, Armenia, Georgia, Kyrgyzstan it was repealed after accession, so the "non-application" principle was invoked, but eventually removed within a year or two. (In the case of Georgia, non-application was never invoked since Jackson-Vanik was removed soon enough after accession.) Only in the case of Moldova does Jackson-Vanik still apply to a country that acceded to the WTO.

Former U.S. Trade Representative Rob Portman testified before Congress in 2006 that the U.S. will have to lift Jackson-Vanik against Russia, Ukraine and Kazakhstan in order for the U.S. exporters and investors to gain the advantages of the commitments these countries are making at the WTO. In the case of Ukraine, Jackson-Vanik was removed in 2006.

VI. Remaining Issues

Often the most difficult issues remain at the end of the accession negotiations. Although Russia has resolved some of the most contentious, (such as gas pricing and branch banking where Russia achieved its objectives in the negotiations) several difficult issues remain.

Georgia--The Customs Posts Issue with Russia

Abkhazia and South Ossetia are two breakaway regions of Georgia that have borders with Russia. Georgia insists that Russia close down two checkpoints between these regions and Russia, and that Russia establish legal customs posts. Georgia believes that a great deal of smuggling is coming from the breakaway regions through the illegal checkpoints and this is helping the breakaway regions to survive.

Russia has banned the import of wines from Georgia, which appears to many Georgian officials as retaliation for the pressure Georgia had placed on Russia in the WTO accession negotiations. Georgia, which has signed its bilateral agreement on Russian WTO Accession in 2004, then withdrew its support for Russia's WTO accession. Moreover, Georgia has objected to the agenda of the multilateral meetings and thereby blocked any meetings of the Working Party on Russian WTO accession. It is very difficult for Russia to resolve the multilateral issues without multilateral meetings.

Article XII of the WTO Articles on Accession states that

"Decisions on accession shall be taken by the Ministerial Conference. The Ministerial Conference shall approve the agreement on the terms of accession by a two-thirds majority of the Members of the WTO."

Based on the two-thirds majority rule on accession in Article XII, Russia has apparently investigated whether it can by-pass Georgia based on this two-thirds majority rule pertaining to accessions. As a practical matter, the two-thirds majority rule is an illusion and all accession decisions are taken by consensus (by unanimity) as are all other decisions of the WTO (except dispute settlement). The Working Party would have to write a final report on Russia's WTO accession, without which the matter of Russia's WTO accession will never come to a vote before the WTO Ministerial Meeting. Just as Georgia has been able to block the Working Party from meeting, Georgia will be able to block the report from going to the Ministerial. So again, consensus is required and Georgia has a blocking vote. This implies that sooner or later Russia will have to negotiate seriously with Georgia, something that Georgian officials have complained has not happened in 2007.

Agriculture

I have discussed this issue above so only briefly discuss it here. Russia failed in the bilateral discussions to achieve its objective of defining 1992-1994 as the base period for trade-distorting agricultural subsidies. Russia now hopes that it will be able to negotiate a dollar amount that it would be allowed to subsidize. This is likely to be a very difficult negotiation as there are other countries, like Kazakhstan and Ukraine, who

would like similar departures from precedent. If the Working Party allows Russia a larger trade-distorting subsidy amount, it will have a more difficult time negotiating previous limits with subsequent applicants for WTO membership. Australia and New Zealand are likely to resist a change in precedent that would allow an increase in the trade-distorting subsidies.

Intellectual Property

In general, the Working Party believes that Russian laws on intellectual property are consistent with international obligations. The problem is in enforcement. In February, U.S. private industry sources complained that Russia was not cracking down on pirated copies of goods, including software, music, films and pharmaceuticals. As part of its bilateral agreement with the U.S., Russia signed a “side letter” in which it agreed to take several steps to strengthen enforcement of its intellectual property regime. Private U.S. industry sources also complain about the failure of Russia to close websites, like allofmp3.com, that sell material that is protected by copyright, and more generally that Russia is not complying with the terms of its side-letter with the U.S. on intellectual property rights.

Issues with the European Union

There are several trade issues between the EU and Russia in the spring of 2007. Although there have been some press reports that allege that the EU is considering blocking Russian WTO accession due to these problems,¹⁴ officially EU officials have not changed their support for Russian WTO accession.

Estonia relocated a Soviet war memorial in its capital of Tallinn. This led to demonstrations at the Estonian embassy in Moscow, and a complaint from NATO that Russia did not protect Estonian embassy staff. This was complemented by a cut off by Russia of oil and coal exports to Estonia. Other issues are the Russian ban on all meat imports from Poland. The EU regards the penalty as disproportionate to the offense of some falsified documents on selected shipments of meat exports from Poland. The EU is also concerned about proposed export taxes on wood exports from Russia and dual pricing for international and domestic rail cargo. On the plus side, one of the more contentious issues, the timing of the elimination of overflight fees for aircraft over Russian skies has been resolved in 2007.

When Will Russia Achieve Membership?

The multilateral talks are focused on the details of how and when Russia will take on the multilateral obligations of a WTO member. Many of the most difficult issues remain to the end of the process and thus some of the most difficult compromises are necessary. Some observers are suggesting that more isolationist interests in Russia have gained more influence and thus Russia is having second thoughts about an open economy

¹⁴ For further details see “EU Threatens Russian Trade Bar,” May 5, 2007. Available at: <http://www.telegraph.co.uk/news/main.jhtml?xml=/news/2007/05/04/wrussia04.xml>

model of economic development. If correct, this would make it very difficult then to come to a final agreement.

Gemain Gref, the Russian minister of economic development and trade, has forecast that Russia should be able to accede to the WTO by the end of 2007. On the other hand, the disputes with the EU have reportedly led some EU officials to express reservations about EU support for Russian unless the problems are resolved. And on February 14, 2007, U.S. Trade Representative Susan Schwab told the Senate Finance Committee that "Russia is not moving ahead with the kind of WTO commitments that it would need, at this point, to become a full-fledged member of the WTO." Regarding the multilateral talks she added they "are not proceeding as well or as quickly as I think Russia had hoped."

The difficulty of the issues above, and the stiffening of political will on many sides (as elaborated by Aslund 2007), suggests that 2007 is overly optimistic for Russian accession. It is difficult to believe, however, that a country as important as Russia will not become a member of the WTO. I am optimistic, therefore, that the West and Russia will eventually come to an agreement. And once Russia has an agreement with the West, Russia and Georgia will also resolve their dispute.

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Table 1: Impact of WTO Accession on Economy-Wide Variables in Russia: Policy Results and Decomposition of Effects (results are percentage change from initial equilibrium)

	Benchmark	WTO accession	Tariff reform only	Improved market access only	Reform of FDI barriers only	WTO accession in steady state model	WTO accession with partial reform of FDI barriers	WTO accession with domestic rent dissipation	WTO accession in short run model
		(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Aggregate welfare									
Welfare (EV as % of consumption)		7.2	1.3	0.6	5.2	23.6	4.1	7.7	5.9
Welfare (EV as % of GDP)		3.3	0.6	0.3	2.4	11.0	1.9	3.6	2.8
Government budget									
Tariff revenue (% of GDP)	1.4	0.9	0.8	1.4	1.4	1.0	0.8	0.9	0.8
Tariff revenue (% change)		-33.4	-38.4	8.4	10.6	-23.3	-35.4	-33.2	-35.8
Aggregate trade									
Real exchange rate (% change)		2.6	2.0	-0.5	1.1	4.8	1.8	2.7	3.0
Aggregate exports (% change)		13.2	7.9	1.5	3.5	24.3	10.8	13.5	9.5
Returns to mobile factors									
Unskilled Labor (% change)		2.5	0.4	0.1	1.9	13.2	1.0	2.7	1.9
Skilled Labor (% change)		4.7	1.5	0.6	2.5	17.6	2.6	4.9	3.4
Capital (% change)		4.9	2.0	0.7	3.1	19.5	3.6	4.9	4.3
Factor adjustments									
Unskilled labor (% of non-sector specific workers who change jobs)		2.6	1.1	0.5	1.6	4.4	1.7	2.6	0.0
Skilled labor (% of non-sector specific workers who change jobs)		2.1	0.4	0.4	1.5	2.5	1.0	2.2	0.0
Capital		0.6	0.4	0.4	0.2	0.1	0.6	0.6	0.4

Source: Jensen, Rutherford and Tarr, Review of Development Economics, August 2007..

Table 2 MFN Tariff rates of the Russian Federation ^(a)

Year	Tariff	Observations	Mean		Standard Deviation		Minimum rate	Maximum rate
			Simple	Trade weighted	Simple	Trade weighted		
2001	<i>Actual MFN tariff rate</i>	11,076	11.7	11.4	10.8	9.5	0	518
	<i>Ad valorem rate only (b)</i>		10.9	10.5	6.0	6.5	0	100
2002	<i>Actual MFN tariff rate</i>	11,148	12.2	13.3	13.7	14.9	0	483
	<i>Ad valorem rate only</i>		10.8	11.2	6.0	8.0	0	100
2003	<i>Actual MFN tariff rate</i>	11,161	12.8	14.3	18.7	18.0	0	1270
	<i>Ad valorem rate only</i>		10.9	10.3	6.9	6.8	0	100
2004	<i>Actual MFN tariff rate</i>	11,218	12.4	14.1	13.3	17.0	0	293
	<i>Ad valorem rate only</i>		10.9	11.1	6.9	7.3	0	100
2005	<i>Actual MFN tariff rate</i>	11,365	12.1	14.0	12.7	15.2	0	470
	<i>Ad valorem rate only</i>		10.8	11.2	7.0	7.8	0	100

Notes: (a) Table 1 presents summary statistics at the ten digit level

(b) The ad valorem rate only calculations ignore specific tariffs, i.e, assume that specific tariffs are zero.

Source: Shepotylo and Tarr (forthcoming).